May 27, 2003

The Honorable Michael K. Powell, Chairman
The Honorable Kathleen Q. Abernathy, Commissioner
The Honorable Kevin Martin, Commissioner
The Honorable Michael J. Copps, Commissioner
The Honorable Jonathan S. Adelstein, Commissioner
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554

Re: Network Economists' Last-Minute Response To Showing In NASA/NAB February 3 Reply Comments

Dear Chairman Powell and Commissioners Abernathy, Martin, Copps and Adelstein:

Fundamentally, the 35% cap is about localism. Throughout this proceeding, the Joint Networks (Fox, NBC and CBS/Viacom) have sought to skew the Commission's focus away from this central principle. Indeed, the arguments advanced by the networks and their economists go beyond simply ignoring localism; they seek to defeat localism:

> **"The Commission's preoccupation with localism is difficult to explain or to justify."[1]**
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> **"The same is true, of course, of the Commission's sometime preoccupation with news and public affairs, as distinct from entertainment programming. This makes even less sense than localism."[2]**
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> **"In the case of broadcasting, network contracts with affiliates have long been constrained [understandably] by various FCC regulations, such as the one that forbids local stations to delegate responsibility for programming decisions."[3]**

Given these attitudes, it is no wonder that the record evidence demonstrates that affiliates serve local community interests better than the network O&Os. Defying reality, the Joint Networks in their latest submission go so far as to claim that NASA/NAB have not conducted any original empirical analysis and have submitted no evidence to the record in support of this cap. In other words, just as the Joint Networks try to denigrate and wish away the statutory mandate of localism, they also ignore the strong body of evidence submitted by NASA/NAB – including the results of an independent affiliate survey, multiple economic analyses, and a variety of other data.

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[1] Comments of Fox Entertainment Group *et al.*, MB Docket No. 02-277 and MM Docket Nos. 01-235, 01-317, and 00-244, Exhibit 3, *Statement on Media Ownership Rules of Dr. Bruce M. Owen*, at 10 (filed January 2, 2003).

[2] *Id.* at 10-11.

[3] Bruce M. Owen *et al.*, *Affiliate Clearances, Retransmission Agreements, Bargaining Power and the Media Ownership Rules* (herein "EI Study"), MB Docket No. 02-277, at 5 (filed April 21, 2003).

The evidence demonstrates a reliable and powerful difference between O&Os and affiliates in terms of local news quality/awards – several analyses demonstrate affiliates are superior; preemptions generally – the networks' own, selective data demonstrate affiliates preempt more; preemptions for community standards – only affiliates ever do this; and incentives and willingness to influence network programming – affiliates' incentives are more closely aligned with local interests and they uniquely exert this influence. In addition, the record contains unrebutted evidence of increased network pressures against local-station preemptions and real-world declines in preemptions over time as a result of such pressures; as NASA has pointed out, network encroachment on affiliate discretion in affiliation agreement provisions and network encroachment on affiliate discretion in terms of network practices; geographic dispersion of ownership among non-network owned stations; innovations on the part of independently-owned stations; availability of affiliates but not O&Os for telethons and charities; and escalating network incentives to subordinate local community needs to conglomerate business strategies.

Against this strong body of evidence, the Joint Networks urge the Commission to focus only on two factors – the number of minutes (and not the quality) of local news carried by O&Os versus affiliates and their desire to make more money by owning more stations.

The Local News Debate: Affiliates Surpass O&Os In Quality And Are Equivalent In Quantity

On May 12, the networks filed yet another economic study *two weeks before the scheduled sunshine date for this proceeding and three and a half months after NASA/NAB placed in the record on the reply comment deadline the facts the new network economists' study attempts to rebut.* The gist of the new economic study is that network O&Os air more local news than independently owned affiliates.

The provision of local news programming is one way, but not the only way, in which local stations serve localism. Unlike the Joint Networks, however, NASA/NAB have not taken the position that the Commission's interest in local news "makes even less sense than localism." Apparently the networks have given up arguing that their O&Os perform as well in news quality using awards as the measure – a measure selected by the Commission as highly relevant. Instead, in their latest filing, the Joint Networks urge the Commission to ignore the superiority of local news quality achieved by independently owned affiliates over O&Os and urge it to focus solely on the quantity of news provided.[4] But as myopic as this perspective would be, the networks' assertions do not stand up even within this constricted field of vision.

<u>The FCC study must be corrected for market size</u> – On October 1, 2002, the Commission released a staff study on news quantity, comparing O&Os and independently owned affiliates, that purported to show the former to be superior. NASA/NAB promptly pointed out that the study failed to correct for market size. Quite obviously, the New York City market (7,282,320 households) generates more news than the Charlottesville, Virginia market (67,490 households). Nor does it require an economist's study to recognize that the networks own a

[4] *Ex Parte* Filing of Fox Entertainment Group *et al.*, MB Docket No. 02-277, at 3, n. 9 and at 4, n. 14 (filed May 12, 2003) ("the FCC should neither evaluate the quality of news nor base any regulations on an evaluation of quality").

disproportionately large number of O&Os in the major markets (ABC, CBS, Fox and NBC own 19 of the 20 affiliated stations in the top five markets), whereas independently-owned affiliates disproportionately serve the smaller markets. In their latest submission, the networks thrice refer to this point as "nitpicking," but it isn't. The flaw is fundamental, and fatal. The networks, themselves, acknowledge that the study must correct for market size.[5]

The Fox statistics alone account for the disparity between affiliates and O&Os – NASA/NAB corrected the staff study for market size, but accepted as reliable the data collected by the Commission's staff. The resulting analysis showed that there is no appreciable difference between the O&Os of ABC, CBS and NBC and their affiliates. As far as we can tell from the numerous network submissions, *the networks do not contest this point either.* The difference as to news quantity found in the FCC study was wholly attributable to disparities between Fox O&Os and Fox affiliates. Obviously, it would be unwise and unreliable to base critical public policy decision on a disparity between affiliates and O&Os that applies to only one of the four major networks. Moreover, the disparities are explained by factors wholly apart from network ownership and, therefore, must be put to one side.

Fox is aberration – Fox is a new network. It has done a remarkable job of building its franchise. Its first step was to acquire stations in the major markets. By and large these were well established stations, like Metromedia's WTTG here in Washington – a VHF station with coverage reach equal to or exceeding its ABC, CBS and NBC affiliated rivals and with a long-running news presence. But in the smaller markets, where for the most part Fox has not chosen to own stations (and where recently it has announced it may divest stations), it affiliated with far weaker stations – weaker in terms of facilities, weaker in terms of frequency, and weaker in terms of news traditions and financial and other resources. No criticism of that strategy is intended; Fox had no choice.

Commission allotment and interference policies explain the differences –A major reason Fox had no choice is the Commission's table of allotments and mileage separation requirements. In the largest markets, the Commission was usually able to allot six or more strong VHF stations (often one of them being an educational station), capable of being located at the most desirable site in the market for providing maximum coverage. But in the majority of the markets, mostly smaller markets, because of mileage separation requirements necessary to protect the public's television service against destructive interference, the Commission was able to allot far fewer optimal VHF channels, and these were already affiliated with the other three networks. As a consequence, 72% of Fox O&Os are VHF stations and only 18% of Fox affiliates are VHF stations.

But Fox affiliates suffer other disadvantages as well, that the Fox O&Os do not suffer. Thus, some are licensed to communities outside of the center of the market. For example, the Fox affiliates in the Cincinnati, OH, Gainesville, FL, and Dothan, AL markets, among others, are licensed to communities outside the market center. Their towers are often not in the most desirable location. For instance, the Fox affiliate in the San Diego market operates on a Mexican frequency, and its transmitter is located on the Mexican side of the border,

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[5] Response of Fox, NBC/Telemundo, and Viacom to Early Submission of NAB and NASA, MB Docket No. 02-277 and MM Docket Nos. 01-235, 01-317, and 00-244, Appendix 1, Bruce M. Owen *et al.*, *News and Public Affairs Programming: Television Broadcast Network Owned and Operated Stations Compared to Network Affiliated Stations,* at 3 (filed December 19, 2002).

25 miles from the tower sites of the ABC, CBS, and NBC affiliates in San Diego. Fox affiliates may not have as much power or height as the other affiliates in the market. In Charlotte, for example, the Fox affiliate has a fraction of the power and only about 60 percent of the height of the NBC affiliate. In some markets, such as Albany, Indianapolis and Denver, the Fox affiliates are the only UHF station, and their big three rivals are all VHF stations, which poses a bigger handicap than if some of the others were also UHFs. They may suffer from receiving antenna orientation problems, which result from a number of the above factors. In addition, Fox affiliates were almost always the weakest stations in the markets, with depleted resources, little or no news traditions and other handicaps. *That's why they were available for affiliation with Fox in the first place.*

<u>Fox had to affiliate with weaker stations</u> – When Fox came onto the scene in the early 1990s, the best three stations in each market were already affiliated with ABC, CBS or NBC. In its affiliation strategy, it had to do the best it could with the remnants and, in addition, to try to "pick off" affiliates of other networks when their affiliation agreements expired. A wavelet of reaffiliation in Fox's favor occurred in the mid-90s, but that aside, Fox has had to make do with weaker affiliates – weaker than the affiliates of the other major networks and far weaker than Fox's O&Os in the major markets which are in essential parity with their ABC, CBS and NBC counterparts. This is the rich, multi-dimensional explanation of why comparing the local news performance of the Fox O&Os and the Fox affiliates is not reliable and should not have been included in the networks' studies.

In its February 3 reply comments, NASA/NAB explained these differences that the networks themselves know to be the truth. The pros at the Commission know them to be the truth. But the networks' economists have trouble with the messiness of reality, preferring to call it names, like "absurd" and "nitpicking." As a consequence, when the networks did their own local news study, they chose simply to disregard all of this clearly pertinent information. Yet the Fox data are the *only* reason for the networks' conclusion that, overall, the networks' O&Os air more local news than the networks' affiliates. NASA/NAB also demonstrated that the FCC's data, once taking into account the skewing effect of the aberrational Fox statistics, show that there is no difference between O&O local news programming and that of affiliates.

<u>The networks' twelfth-hour filing does not satisfactorily address the NASA/NAB points</u> – The networks' May 12 submission (economists' study at 6) argues for "controlling for any variation in the hours of local news programming that might be attributable to the frequency band," rather than setting aside the Fox statistics. Accordingly, in presenting their alternative analysis, the network economists claim to have taken into account the VHF/UHF disparity which they concede is statistically significant (though we do not have access to the underlying information used by the networks and, therefore, cannot test or replicate it). This step, however, does not take into account all the other respects in which the Fox data are unique because, unlike the affiliates of the other networks, the Fox affiliate line-up differs radically in a variety of ways from the Fox O&Os. Unless and until the network economists can come up with a methodology that takes into account all the factors that create the significant skewing effect of the Fox data – which they have not done – the *only* legitimate way to deal with the Fox O&O/affiliate differential is to exclude it from the comparison.

The Commission Has A Congressional Mandate To Serve Localism – It Is Not Charged With Optimizing Network Profit And Efficiency

The second "new" argument advanced by the networks in their May 12 filing is a series of quotations from the economic "study" it submitted on February 3, 2003. The gist of these quotations is that the national cap gets in the way of efficiency. But the *Fox* Court had already dismissed this line of advocacy.

> This paean to the undoubted virtues of a free market in television stations [that the networks have urged] is not, however, responsive to the question whether the Congress could reasonably determine that a more diversified ownership of television stations would likely lead to the presentation of more diverse points of view. By limiting the number of stations each network (or other entity) may own, the NTSO Rule ensures that there are more owners than there would otherwise be. *An industry with a larger number of owners may well be less efficient than a more concentrated industry. Both consumer satisfaction and potential operating cost savings may be sacrificed as a result of the Rule. But that is not to say the Rule is unreasonable because the Congress may, in the regulation of broadcasting, constitutionally pursue values other than efficiency . . . .*[6]

Just as the network economists don't begin to understand the difference between the Fox O&Os and the Fox affiliates or between the Fox affiliate body and the affiliates of the other three networks, so too have the networks wholly failed to understand what this aspect of the proceeding is all about, what the 1996 Act was all about, what the Court remand was all about and what the Communications Act is all about. The Commission could have created a "more efficient" national system of huge broadcast stations covering the entire United States and not bothered with locally based stations. Congress's mandate to the Commission did not allow that – which is why the Commission may not raise the cap by downgrading the importance of localism as the networks would have it do.

Repeating The Same Old Fallacies Doesn't Make Them True

The networks' last-ditch filing contains some of the old canards.

- It seeks to elevate the standard set by the *Fox* Court as "insurmountable," whereas the Court itself said that it was likely that the FCC could meet it. If the Court had intended an insurmountable standard, it would instead have written a very different decision and vacated the rule, as it did the TV/cable cross-ownership rule.

- It unaccountably criticizes NASA/NAB for not coming forward with sufficient evidence when as shown in our April 22 letter, NASA/NAB's

[6] *Fox Television Stations, Inc. v. FCC,* 280 F.3d 1027, 1047 (D.C. Circ. 2002) (emphasis added).

evidence far exceeds what the networks have submitted, covers at least 12 different issues, and is often unrebutted. The networks focus on only one of those evidentiary issues (quantity of local news), wishing perhaps that the Commission would overlook the other 11 issues.

- This same criticism is particularly hypocritical in view of the networks "hide-the-ball" strategy with respect to preemption data, which only the networks possess and which five months ago the Commission said it expected the networks to disclose – an expectation that turned out to be in vain.

- The networks remain silent about the NASA/NAB economists' analyses that demonstrate beyond a doubt that the network objectives of serving broad corporate business objectives incentivize their O&Os to give short shrift to local community needs.

* * *

As set forth in NASA/NAB's filing of April 25, whatever decision the Commission ultimately reaches in this proceeding – retention, relaxation or repeal of the 35% cap – must be shown on the public record to serve the public interest. Neither relaxation nor repeal meets that test. As for retaining the 35% cap, the evidence is far stronger in support of it today than when Congress adopted it in 1996.

Respectfully submitted,

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